OFFICE OF INSPECTOR GENERAL
UNITED STATES POSTAL SERVICE

January 16, 2009

LYNN MALCOLM
VICE PRESIDENT, CONTROLLER

SUBJECT: Audit Report – Fiscal Year 2008 Postal Service Financial Statements Audit – Washington, D.C., Headquarters (Report Number FT-AR-09-007)

This report presents the results of our audit of the fiscal year (FY) 2008 Postal Service financial statements – Washington, D.C., Headquarters (Project Number 08BM004FT000). The Postal Reorganization Act of 1970, as amended, requires annual audits of the Postal Service's financial statements. We conducted this audit in support of the independent public accounting (IPA) firm's overall audit opinion on the Postal Service's financial statements. This audit addresses financial risk. See Appendix A for additional information about this audit.

Conclusion

During our audit at the Washington, D.C., Headquarters, we noted:

- Financial accounting policies and procedures provided for an adequate internal control structure and conformed with accounting principles generally accepted in the U.S.
- Accounting transactions at headquarters[1] affecting general ledger (GL) account balances were stated in accordance with accounting principles generally accepted in the U.S.
- GL account balances for unemployment liability and expense conformed to the general classification of accounts on a basis consistent with that of the previous year.
- The Postal Service complied with laws and regulations that have a direct and material effect on the financial statements.
- No adjustments were proposed.
- We identified a control deficiency regarding manual journal voucher processing.

[1] The U.S. Postal Service Office of Inspector General (OIG) and the IPA coordinate testing and review of significant headquarters accounts and manual journal vouchers (JV).

This item was not significant to the financial statements and did not affect the overall adequacy of internal controls.

Manual Journal Voucher Processing

Management did not always maintain adequate controls over JV preparation, approval, and review. Of the 415 manual JVs reviewed, we found 16 (with entries totaling approximately $571 million) that had internal control deficiencies. In our previous audit,[2] we identified the same or similar internal control issues within this process. Management reiterated the JV internal control procedures to all applicable personnel in January 2008. However, the table below shows that in addition to the two newly identified issues (yellow shading), we found management had still not resolved two of the six previously reported issues (gray shading).[3] See Appendix B for manual JV details.

Timeframe of JV					Internal Control Issue	Instances In FY 2007
Qtr 1	Qtr 2	Qtr 3	Qtr 4	Total		
--	--	--	1	1	No evidence of "entered by"	--
--	1	--	7	8	Staff members approved JVs their managers prepared	--
--	2	--	--	2	Some or all support missing	5
4	1	--	--	5	No evidence of final approval put into the *Journal Entry Vehicle* (JEV)[4] or posted to the GL	1

Postal Service policy[5] states accounting practices at headquarters are expected to be consistent with general fundamental internal control principles, including proper explanation, support, and approval of JVs. Also, Corporate Financial Reporting (CFR) has informal procedures over JV processing.

[2] *Fiscal Year 2007 Postal Service Financial Statement Audit – Washington, D.C., Headquarters* (Report Number FT-AR-08-006, dated February 8, 2008).
[3] Control deficiencies identified in FY 2007 that we did not identify again in FY 2008 were (1) preparer not identified, (2) no evidence of approval, (3) no evidence of review, and (4) JV amount differed from amount stated in supporting documents by $100.
[4] The JEV application provides a method for entering JVs into the General Ledger Accounting and Financial Reporting System. The application allows users to create, save, edit, and approve or reject manual JVs.
[5] Handbook F-1, *Accounting and Reporting Policy*, dated July 2008.

We were not able to identify a primary cause for the various errors. However, it appears as though human error, as well as inadequate oversight, continue to be contributing factors. This situation increases the risk of misstated financial information in the GL. See Appendix C for our detailed analysis of this issue.

We recommend the Vice President, Controller, direct the Manager, Corporate Accounting, to:

1. Develop formal written procedures for manual journal voucher processing and distribute to all applicable personnel.

Management's Comments

Management agreed a formally documented policy is a sound practice. A formal written policy will be developed and distributed by June 30, 2009. This will include policy requiring the JV approver to be senior to the preparer.

Management stated all of the manual JVs tested during the audit were proper and booked correctly and, although some JVs were reviewed by persons at levels junior to the preparer, there was no evidence any control procedures were not properly performed – only that documentation of the performance of these controls was incomplete. Management further asserted it is inappropriate for the OIG to imply controls are not in place and there is increased risk of misstated financial statements. They said this implication fails to acknowledge the existence of compensating controls, including senior management's review of monthly financial reports that serve to mitigate significant potential errors that would occur in preparing manual JVs.

See Appendix D for management's comments, in their entirety.

Evaluation of Management's Comments

The OIG considers management's comments responsive to the recommendation and corrective actions should resolve the issues identified in the report. Management agreed with the intent of the recommendation and plans to develop and distribute formal procedures by June 30, 2009.

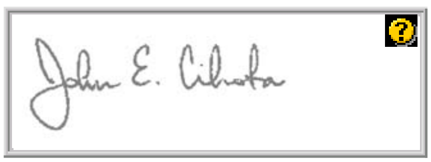
We acknowledge the manual JVs tested during the audit were proper and booked correctly. However, we still maintain there was inadequate support for the two JVs. We do not view our statement and conclusion on controls as contradictory. The intent of the statement regarding ". . . internal controls not in place. . ." is to show, in general, the potential effect when internal controls are not in place and effective. We do acknowledge the existence of compensating controls; however, our focus was to highlight deficiencies at this control point in the overall process.

Observation

We observed the following issues during our JV review that were not material to the overall financial statements and did not affect the overall adequacy of internal controls over JV processing. We observed these same issues during FY 2007.[6] We found significant improvement with one of the issues identified, as shown in the table below.

JV Entry Process Issue	Number of Instances in FY 2008	Number of Instances in FY 2007
Inconsistent Evidence of Approval for JVs that were Prepared and Approved by Another Office	2	14
“Approver” and “Entered By” was the Same Official	3	2

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, please contact Lorie Nelson, Director, Financial Reporting, or me at (703) 248-2100.



John E. Cihota
Deputy Assistant Inspector General
for Financial Accountability

Attachments

cc: H. Glen Walker
Vincent H. DeVito, Jr.
Stephen J. Nickerson
Katherine S. Banks

[6] In FY 2007, we also observed two instances where JV amounts differed from control sheets. However, we did not identify any instances during FY 2008.

APPENDIX A: ADDITIONAL INFORMATION

BACKGROUND

U.S. Postal Service Headquarters Finance establishes accounting policies and provides guidelines for recording and reporting Postal Service financial transactions. Internal control and reporting systems have been created to ensure management and the public receive meaningful financial information in accordance with generally accepted accounting principles. We conducted this audit in support of the IPA's overall audit opinion on the Postal Service's financial statements.

We will issue separate financial statements audit reports for the Eagan, MN; San Mateo, CA; and St. Louis, MO, Information Technology and Accounting Service Centers (IT/ASCs). Further, in addition to the overall opinion on the Postal Service's financial statements, the IPA, contracted by the Board of Governors to express an opinion on the financial statements, will issue separate reports on the Postal Service's internal controls and compliance with laws and regulations. The OIG will also issue a separate report for the audit of the FY 2008 information system controls at the Eagan, San Mateo, and St. Louis IT/ASCs; and the Raleigh, NC, Information Technology Service Center.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objectives of the audit were to determine whether:

- The financial accounting policies and procedures provide for an adequate internal control structure and comply with accounting principles generally accepted in the U.S.

- Accounting transactions at headquarters impacting the GL account balances for assets, liabilities, equity, income, and expenses of the Postal Service are fairly stated in accordance with accounting principles generally accepted in the U.S.

- GL account balances conform to the general classification of accounts of the Postal Service on a basis consistent with that of the previous year.

- The Postal Service complies with laws and regulations that have a material and direct effect on the financial statements as a whole.

To accomplish our objectives, we conducted fieldwork from December 2007 through November 2008. We have a memorandum of understanding with the IPA regarding our responsibilities for testing and reviewing internal controls and processes and significant headquarters accounts (cash, investments, workers compensation, and unemployment liability), manual JVs,[7] and laws and regulations. Further, we verified the Board of Governors' travel and miscellaneous expenses totaling $116,241 and external professional fees totaling $6,703; and tested and accepted officers' travel and representation expenses totaling about $1.2 million. We are issuing separate reports for our audits of the FY 2008 Board of Governors' travel and miscellaneous expenses and of the FY 2008 officers' travel and representation expenses.

We conducted this audit from December 2007 through January 2009 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to limit audit risk to a low level that is, in our professional judgment, appropriate for supporting the overall audit opinion on the financial statements. Those standards also require us to consider the results of previous engagements and follow up on known significant findings and recommendations that directly relate to the objectives of the audit.

An audit also includes obtaining a sufficient understanding of internal control to plan the audit and to determine the nature, timing, and extent of audit procedures. We supported the IPA in obtaining reasonable assurance about whether the financial statements are free of material misstatement (whether caused by error or fraud). Absolute assurance is not attainable because of the nature of audit evidence and the characteristics of fraud. Therefore, an audit conducted in accordance with generally accepted government auditing standards may not detect a material misstatement. However, the IPA and the OIG are responsible for ensuring that appropriate Postal Service officials are aware of any significant deficiencies that come to our attention. We discussed our observations and conclusions with management on December 15, 2008, and included their comments where appropriate.

We relied on computer-generated data from several Postal Service financial systems, including:

- eTravel System
- Chase Insight
- Workers' Compensation Master File
- Accounting Data Mart (ADM)

We performed specific internal control and transaction tests on these systems' data, to include tracing selected financial information to supporting source records. For example, we tested the reliability of the Workers' Compensation Master File by comparing the system's data to a random sample of 60 case files.

[7] Statement on Auditing Standards (SAS) No. 99, *Consideration of Fraud in a Financial Statement Audit*, requires auditors to perform certain tasks to address the risk of management override of internal control. To address such situations, SAS No. 99 requires auditors to test the appropriateness of journal entries recorded in the GL and other adjustments.

PRIOR AUDIT COVERAGE

Report Title	Report Number	Final Report Date	Monetary Impact	Report Results
Fiscal Year 2007 Postal Service Financial Statements Audit – Washington, D.C., Headquarters	FT-AR-08-006	2/8/08	N/A	We identified a control deficiency regarding manual JV processing. We recommended management reiterate JV internal control procedures to all applicable personnel, and management did so in January 2008. However, we continue to find the same or similar issues. See the "Manual Journal Voucher Processing" section of this report.
Fiscal Year 2006 Postal Service Financial Statements Audit – Washington, D.C., Headquarters	FT-AR-07-004	12/7/06	N/A	We did not report any findings or provide any recommendations.
Fiscal Year 2005 Postal Service Financial Statements Audit – Washington, D.C., Headquarters	FT-AR-06-002	11/16/05	N/A	We did not report any findings or provide any recommendations.

For all 3 years, we found management's financial accounting policies and procedures conformed to accounting principles generally accepted in the U.S. and provided for an adequate internal control structure. In addition, GL account balances for investments, unemployment compensation, and Governors' and officers' travel and expenses were stated in the national trial balance in accordance with accounting principles generally accepted in the U.S. Further, we did not identify any instances of noncompliance with laws and regulations that have a direct and material effect on the financial statements.

APPENDIX B: MANUAL JOURNAL VOUCHER DETAILS

	JV#	Month	JV Amount
No evidence of (1) final approval signature, (2) input into JEV form, or (3) staging for posting to the [redacted][8]			
1	117.0	Dec. 2007	$149,676,099
2	957.6	Dec. 2007	8,195,822
3	958.1	Dec. 2007	14,995,468
4	964.0	Dec. 2007	3,000,000
5	965.9	March 2008	45,000,000
			$220,867,389
Staff members approved JVs prepared by their managers			
1	958.4	March 2008	$49,000,000
2	957.5	July 2008	5,270,000
3	959.2	July 2008	8,500,000
4	959.6	July 2008	7,600,000
5	956.2	Aug. 2008	146,100,000
6	957.0	Aug. 2008	4,300,000
7	958.4	Aug. 2008	5,270,000
8	960.0	Aug. 2008	7,400,000
			$233,440,000
Some or all support missing			
1	960.2	Feb. 2008	$60,000,000
2	960.7	Feb. 2008	40,000,000
			$100,000,000
No evidence of JV "entered by"			
1	964.4	Sept. 2008	$16,817,658
16			**$571,125,047**

[8] [redacted]

APPENDIX C: DETAILED ANALYSIS

Internal controls over manual JVs processed by CFR were generally adequate and served a legitimate business purpose. However, CFR did not always comply with controls over manual JV preparation, approval, and review. Specifically, of the 415 manual JVs reviewed, 16 (with entries totaling more than $571 million) had one or more internal control deficiencies.

The General Ledger Accounting and Financial Reporting System includes a process for entering manual accounting journal entries into the GL. The manual JV process begins with the need to capture financial information in the GL or the occurrence of a business activity.

CFR personnel prepare both manual recurring[9] and non-recurring[10] journal entries. CFR uses Postal Service Form 824, *Journal Entry Form*, to track all manual JVs processed through the JEV application. The JEV forms are in an Excel spreadsheet format; include a description of the journal entry, preparer, JV number, dollar amount, and date prepared; and are entered into the GL. For FY 2007, CFR prepared 578 manual JVs with entries totaling approximately $48 billion. For FY 2008, CFR prepared 588 manual JVs with entries totaling approximately $41.4 billion.

Postal Service policy covers accounting and reporting practices and states accounting practices at headquarters are expected to be consistent with general fundamental internal control principles, including proper explanation, support, and approval of JVs. However, we found a manager and team lead accountant prepared eight JVs approved by their staff members. For example, in one instance, the CFR manager prepared a JV that was then approved by a manager reporting directly to him. In addition, two JVs did not have sufficient documentation to support them.

Handbook F-1 covers accounting and reporting practices and Handbook F-20, *General Ledger Accounting and Financial Reporting System,* Chapters 2 and 5, covers manual JV processing. In addition, CFR supplements these handbooks with additional informal procedures as follows.

1. Personnel prepare JVs with documentation justifying the entry and supporting the finance numbers, account numbers, and dollar amounts. The preparer initials the JV form as "Prepared By."

2. A different individual reviews and approves the JV and accompanying documentation. This individual initials the JV form as "Approved By."

[9] Recurring journal entries have the same accounts and/or amounts and recur from month to month.
[10] Non-recurring journal entries are initiated by CFR to reverse journals, month-end accruals, and reclassification entries.

3. An individual then determines whether the JV has proper approval, enters it into the JEV, saves the data entry, and initials the JV form as "Entered By."

4. An individual different from the one entering the JV into the JEV reviews the data entry and, if approved, initials the JV form as "Reviewed By."

5. Upon approval, the individual that entered the JV into the JEV electronically submits the JEV data to a senior accountant for final review and preparation for posting into the GL. The individual then writes the letter "S" on the JV.

6. The team lead accountant performs an overall final review of the JV and its input into JEV. Upon completion, the team lead accountant moves the JEV entry for posting into the GL. The team lead accountant then writes "M" on the JV.

7. Eagan IT/ASC personnel post the JEV entry into the GL.

8. The individual from headquarters (step 3 above) reviews the GL the next day to verify the JV entries were posted to the GL and are accurately reflected in ADM. The individual documents this verification with a notation of "POSTED" on the JV.

The Postal Accountability and Enhancement Act, passed in December 2006, requires the Postal Service to comply with applicable portions of the Sarbanes-Oxley Act by 2010. Accordingly, the Postal Service must be able to detect and prevent misstatements timely and be assured that internal control procedures are designed and maintained to ensure material information is disclosed. When internal controls over manual JV processing are not in place, there is increased risk of misstated financial information in the GL.

APPENDIX D: MANAGEMENT'S COMMENTS

LYNN MALCOLM
VICE PRESIDENT, CONTROLLER

UNITED STATES
POSTAL SERVICE

January 9, 2009

LUCINE M. WILLIS

SUBJECT: Fiscal Year 2008 Postal Service Financial Statements Audit – Washington, D.C. Headquarters (Report Number FF-AR-09-DRAFT)

Thank you for the opportunity to review and comment upon the draft audit report issued December 26, 2008. We are pleased to note that the financial accounting procedures employed at the headquarters location are adequate and that the accounting transactions recorded at headquarters were stated in accordance with generally accepted accounting principles.

The recommendation in the report and our response are found below.

Recommendation

Develop formal written procedures for manual journal voucher processing and distribute to all applicable personnel.

Response

Although the oversights identified in the report with respect to documentation of approvals on manual journal vouchers were due to human error, rather than the lack of a written policy, management agrees that a formally documented policy is a sound practice. A formal written policy will be developed and distributed by the June 30, 2009. This will include policy requiring that the JV approver be senior to the preparer. This was not previously specified and accounted for half of the items noted in the audit.

It must also be pointed out that all of the manual JVs tested during the audit were proper and were booked correctly. Although some JVs were reviewed by persons at levels junior to the preparer, there is no evidence that any control procedures were not properly performed, only that documentation of the performance of these controls was incomplete. The two JV's identified to be missing supporting documentation were, in fact, properly supported; however the documentation was filed separately from the JV.

475 L'ENFANT PLAZA SW RM 8011
WASHINGTON DC 20260-5200
202-268-4177
FAX: 202-268-6934
WWW.USPS.COM

- 2 -

It is therefore inappropriate to imply, as is done in the last paragraph of appendix C, that controls are not in place and that there is an increased risk of misstated financial statements. This implication fails to acknowledge the existence of compensating controls, including senior management review of monthly financial reports that serve to mitigate significant potential errors that would occur in preparing manual JVs. This statement in Appendix C, contradicts the OIG's own conclusion on page two of the report that "This item was not significant to the financial statements and did not affect the overall adequacy of internal controls."

We do not believe that this report contains any propriety or business information and may be disclosed pursuant to the Freedom of Information Act.

Lynn Malcolm

Lynn Malcolm

cc: Kathy Banks